CORPORATE ALLERGY. SIGNS AND TREATMENT

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Processes occurring in human body are well suited for the understanding of the key strategic business processes taking place in a corporation. Thus allergies that a person may experience are alike unfortunate condition of companies while merger and integration.
According to medical definitions, allergy is an immune response to substances that enter or come in contact with the body causing irritation and rejection. The same reaction a company may induce in an M&A deal being implemented in other entity. In this article, we will focus on the corporate allergies or rejection of business structures in mergers and acquisitions.

Key words: corporate allergy, M&A, growth model, market capitalization.

Nowadays there are four major trends that characterize modern business environment: globalization, integration, specialization and capitalization. Market capitalization has the particular importance in terms of international business development and marks the transition from the priority of operating income to the concept of long-term business growth. A way from profits to the value of the company is a key development track of the business in today's market cap oriented world. However, a long-term increase in capitalization is assured by a positive dynamics of profit before tax (EBITDA), which, in turn, is achieved through the so-called «Crocodile Mouth Effect» (the author's terminology). The «Crocodile Mouth Effect» occurs in the circumstances of multidirectional dynamics of net revenue (NSR) and operating costs (Cost Of Operations). Thus, rising net revenue and descending on operating costs created «Crocodile Mouth

Effect». Difference achieved is a positive, cumulative EBITDA that largely determines the value of the company in the long term.

In modern conditions of development of corporate business it is getting more challenging to ensure the increase in net revenues and at the same time the reduction of operating costs. An increasing number of companies are moving from growth model to models of optimization and rationalization of operating costs of business, working on stagnating saturated markets. This is a situation when revenues are not growing or have a conditional growth of 1-2%, with the cost reduction program implemented. This leads to the already mentioned positive EBITDA, which supports the growth trend of the business without increasing the capitalization of the company itself.

Modern transnational corporations demonstrate alternative growth models. Among alternative growth models which we highlight the following: organic growth, guaranteed growth and growth through M&A.
The first alternative growth model is organic growth. In the frame of this scenario the company's growth is ensured by the development of new products or services, new markets opening, new channels of sales. Here we deal with about business' opportunities for self-generation of growth factors.
The second alternative growth model is guaranteed growth. Development of the company largely depends on its interaction with a sustainable business partner and stable conditions such as government orders or a model of feeder business, when the company throughout its existence provides services for a big customer, being thus its implant business.
The third growth model is growth through mergers and acquisitions (M&A). This is the stage of development of corporate business, where further growth is largely dependent on the company's ability to implement mergers and acquisitions. At this stage it's easier for a company to buy a manufacturer of technologies, products and services, rather than to provide independent development of its own. M&A is an effective tool for a rapid growth in saturated markets and quick access to new markets.

Figure 1. Global M&A from 2005 to 2014.

Figure 1 shows the dynamics of global mergers and acquisitions market. World GDP in 2014 amounted to approximately 77,9 trillion dollars (according to the World Bank), ie, the share of M&A market in 2014 amounted to 4% of global GDP. In 2014, global deal value increased at a much higher rate than deal volume, largely caused by a large number of mega-deals. We suppose that with the strengthening of the factors of the global economic crisis and the slowdown in global GDP growth M&A market will develop further and take a greater share in the global GDP. It is becoming more challenging for companies to compete in the "frozen", falling markets. Creating new markets and developing new competences is becoming more difficult and requiring more investments. Thus mergers and acquisitions are getting an efficient tool for growth achievement ensuring corporate growth through redistribution of market shares and its consolidation.

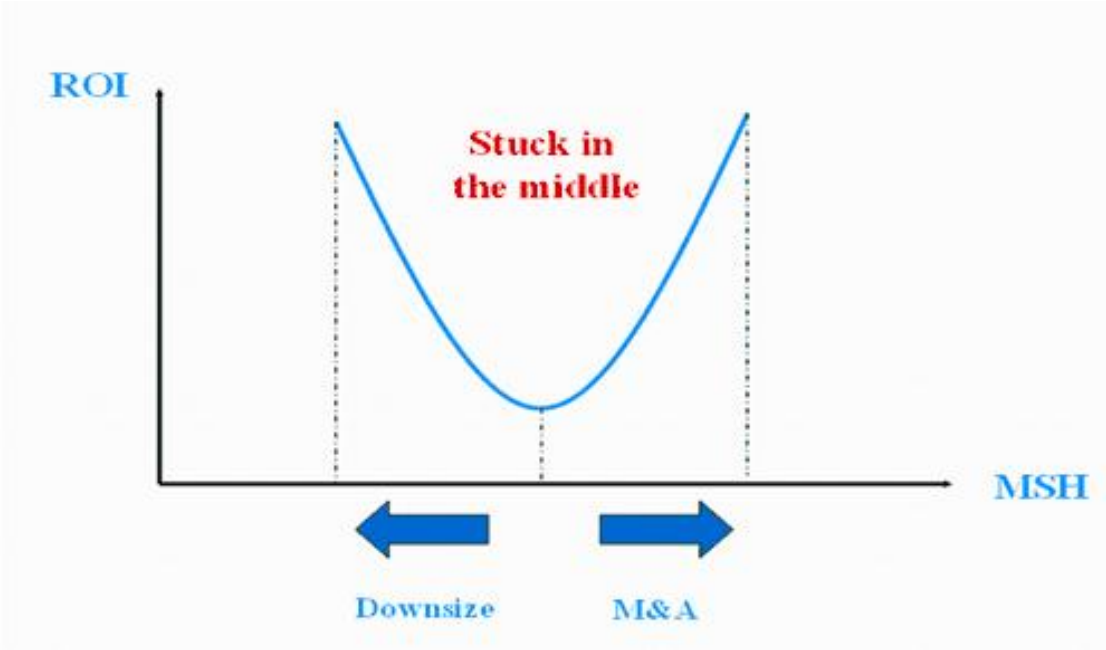

Figure 2. Paths of business development.

Figure 2 describes the real situation faced by the majority of businesses throughout their lives. We show a coordinate system with two indicators which are return on investment (ROI) and market share (or turnover). The price for increasing of presence in the market is paid by increasing costs and reinvesting profits into development. The income on investment of shareholders in the business fall and reach the so-called "corporate bottom" when the ROI falls below the average deposit rate of commercial bank. Shareholders find themselves at the crossroads. They can either go out of business or move on. One of the alternatives is coming back to the previous rate of return up to its fall mark is a strategy of downsizing (reduction operations and deep concentration on its core competence). Another alternative is to continue increasing its market share through the acquisition of new assets through M&A activities, capable to ensure the restoration of profitability indicators. In this regard, mergers and acquisitions are becoming an important alternative tool for the company's

growth and meeting the expectations of the shareholders on the performance of business profitability.

A vivid example of the downsizing is the experience of the Marks & Spencer Company. After a long and exhausting competition with the Inditex Group, hitting a level of corporate bottom, Marks & Spencer decided to reduce its operations and focus on core competencies manufacture and sale of goods from wool. At the same time a large part of the corporate business is developing through mergers and acquisitions, e.g. Coca Cola, PepsiCo, Wall Mart, Unilever.

Thus, the global corporate business in general is following the M&A path of the development. Transactions are being made, the structures are being integrated together, companies are looking for synergies and additional points of growth. However, in fact, many transactions are completed only on paper. Companies fail to get united and merge into a single corporate structure. There is a rejection of structures that is alike an effect of mixing water and butter. Due to significant differences in nature these substances do not merge.

Let's concentrate on causes and symptoms of corporate allergies and mismatch.

1. Businesses are not compatible at all. Business structures specializations are not relevant to each other and integration does not seem to be realistic. An attempt to turn the horizontal diversification into vertical integration often leads to a negative result.
2. Blurring the focus of a combined company. This point implies a dramatic increase in the combined product portfolio. At the same time top management does not place a priority in the implementation and production. The system becomes complex and not controllable.
3. The complexity of business processes and technologies to the perception of business structures.
4. Multidirectional relation to the merger of management of two companies involved in the transaction.
   Figure 3 shows attitude to the deal of the members of the corporate management structure (the top management of the company A, company B, the management company A, company B). Even with positive attitude of top management to the deal, the middle and lower management levels with a negative attitude to the merger, sabotaging the work of the program, contribute to the disruption of the merged business structures. Conversely, the negative attitude of top management, an inhibitory decision with full respect to the positive management of lower links lead to the same result. Negative background can be a feature of the new people's fear. At this point it is very important to understand who is the object, and who the subject of a takeover. Often the scavenger strives to get rid of staff of the absorbed company, thereby compromising the career expectations of staff of the latter.

CEO A	Co A	CEO B	Co B	Сценарий
Positive +	Positive +	Positive +	Positive +	Scenario 1
Positive +	Positive +	Positive +	Negative -	Scenario 2
Positive +	Positive +	Negative -	Negative -	Scenario 3
Positive +	Negative -	Negative -	Negative-	Scenario 4
Negative -	Negative -	Negative -	Positive +	Scenario 5
Negative -	Negative-	Positive +	Positive +	Scenario 6
Negative -	Positive +	Positive +	Positive +	Scenario 7
Negative -	Positive +	Negative -	Positive +	Scenario 8
Negative -	Positive+	Positive +	Negative -	Scenario 9
Positive +	Positive +	Negative -	Positive +	Scenario 10
Positive +	Negative -	Positive +	Negative -	Scenario 11
Positive +	Negative -	Negative -	Positive +	Scenario 12
Negative -	Negative -	Negative -	Negative -	Scenario 13

Figure 3. Management's attitude to the deal.

5. Cultural intolerance, rejection of corporate culture. This happens due to the collision of different management style, values, corporate culture and values, personal believes.

Symptoms of corporate allergies that can affect the entire company or a part of the functional area are common for all companies. These signs may include reduction in revenues and increase in operating expenses. As a result, the "disease" leads to the situation when the capitalization, turnover, profitability combined structure are less than that the absorber had before making mergers and acquisitions.

Case:
A prime example of the corporate practice of allergy symptoms is the deal on the acquisition of the American company AOL of a progressive service Bebo. In 2008, AOL paid for Bebo 850 million USD, but in 2010 it sold for 10 million USD. The deal failed due to inability to successfully integrate the target company for the development of its own social network and resource competition with emerging network Facebook.

Here are some recommendations aimed to avoid corporate allergy.

1. Avoid one-time purchase of 100% of equity of the asset. The path to the control of the company should begin with a gradual build-up of ownership, and thus, to ensure the gradual integration of management into united business processes. Today it is a common practice when companies arrange the so-called "deal of mutual exchange of shares» (mutual stock owning), that turn to be a kind of "trial period".
2. Mergers and acquisitions in the case of high-risk corporate allergy may be replaced by a strategic alliance or association without legal associations

(legal) forms. TNK and BP, Danone and Unimilk are successful examples of such methods. In this case companies remain independent internationally, but in specific markets provide companies with an equal form of ownership.

3. Annihilation. Mergers and acquisitions preserve the independence of the business structures through their division on the basis of forms of specializations, each of which has continued its independent capitalization and can act subsequently isolated structure of the subject / object of M&A.
4. The use of different methods of practice (trainings, team buildings) adaptation of the personnel to the new, combined company. It is necessary to eliminate the perception people have of the transaction as a "strong overtakes the weak." Both the target and the buyer structure should be equally represented. The employees should be equally evaluated according to unified rules and regulations. Often, jobs in the context of operating synergies are distributed not on the basis of professional competence. M&A transactions ought to become a professional assessment, not only for those who has been bought, but for those who acquires. This principle would ensure fair competition and effective team creation.
5. Development of a new corporate culture. This is a wide spread mistake to assume that corporate culture does not change in M&A. We propose the idea of creating the new culture that appears as a result of M&A, based on the success factors and values that two companies have.

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